News

Chinese apparel industry repositioning for growth?

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A massive shake-out is taking place in the Chinese apparel industry, as firms struggle to remain competitive against a backdrop of rising labour costs, the strengthening of the yuan, worker shortages and tighter pollution controls. However, as Jozef De Coster reports, some companies are re-positioning to get their businesses back on track.

The transformation of China's textile and apparel industry is likely to continue for some time, cutting jobs by the hundreds of thousands – the restructuring of Weiqiao alone, China's largest cotton textile enterprise, made 17,000 workers redundant.

On the other hand, it's widely believed that the present crisis will result in a more efficient apparel industry, better adjusted to meeting demand in foreign and domestic markets.

However, the falling international competitiveness of the Chinese apparel industry is in marked contrast to that of the country's economy as a whole.

According to the Global Competitiveness Report 2008-2009 from the World Economic Forum, China entered the Top 30 in 2008, up four places from the year before.

The country benefits from its large and rapidly growing foreign and domestic markets, allowing for significant economies of scale. Macroeconomic stability also remains a source of competitive advantage, while innovation is becoming a new one.

But as far as the apparel industry is concerned, there's unanimity that it's losing its edge.

Negative factors At last autumn's Intertextile Shanghai Apparel Fabrics trade fair, representatives from the clothing industries in Vietnam, Cambodia and Laos, all said they expect to benefit from China's declining competitiveness.

Indeed, a number of factors are undermining China's competitive superiority.

- Rising labour costs. According to Textiles Intelligence, Werner International data shows the average annual increase in Chinese labour costs over 2004-2007 was 11.8% in the coastal region and 14.6% inland.
- In 2008, Chinese labour costs are expected to have risen by 20-25%. Stringent labour laws introduced in January 2008 stipulate a minimum wage and fixed overtime, severance pay, health and accident care and a pension

plan for workers. Credit Suisse eestimates that these laws alone add 15-20% to the cost of running a labour-intensive industry, and for small and medium-sized apparel exporters they come at a rough time.

- The strengthening of the Chinese yuan, especially against the Euro. From the beginning of July until the end of October 2008, the yuan rose almost 24% against the Euro. As most Chinese apparel exporters apply razor-thin profit margins, such changes in foreign exchange can prove deadly.
- Rising costs of raw materials such as cotton, polyester and wool. In 2007 alone the cost of cotton imports rose about US$286 per ton.
- Higher tax rates in several regions. In Shenzhen, a major apparel production centre close to Hong Kong, the tax rate for processing and manufacturing companies was 15%. Now it's 25%.
- Shortage of workers. Improving employment prospects in rural areas and inland cities, coupled with the rising cost of living in the Pearl River Delta, Guangdong and the Yangtze River Delta, mean many of China's estimated 210m migrant workers are choosing to stay closer to home.

  Many garment factories can't find enough workers, even if they are offering pay rises in excess of 10%.

  Michel Boogaers, CEO of Hong Kong-based Able Glad, a manufacturer of sports, casual and ski-wear, with factories in Dongguan and Shaoxing, says both factories now have to operate with 800 workers each instead of the usual 1,000.

  Other apparel producers who are in need of workers are reportedly cutting in their customer base, especially shunning customers who in the past imposed "unrealistic" social compliance requirements.
- •Tighter pollution regulations and other environmental requirements. Companies are pressed to invest in expensive new machinery and improve their waste-management systems. Chinese officials can be ruthless on environmental matters, and in mid-2007 vowed to simply eliminate some 2,150 polluting firms by the end of 2008.
- Banking restrictions. Neither the global financial turmoil nor recent company break-downs in the Chinese textile supply chain (from key suppliers like PTA-producer Sanxin to thousands of apparel makers) were able to convince Chinese banks to relax their credit policy for the apparel industry – an industry they traditionally approach with caution.

Eight strategies to get back on track Hans De Gusseme, the commercial director of weaving machinery builder Picanol (Suzhou), has a privileged outlook on developments in the Chinese textile and apparel supply chain and is fully aware of the seriousness of the crisis rocking the industry.

Yet he's confident the combined efforts of the Chinese government – which has already raised export tax rebates for garments and textiles from 11% to 17% and is mulling a new stimulus package for the sector – and individual companies will succeed in re-shaping the industry.

He believes that if the industry is able to operate higher in the value chain, it will offer competitive advantages in both domestic and international markets.

The following are eight re-positioning strategies currently applied by Chinese apparel companies.

- Relocating production. Some apparel producers are relocating to other regions in China with lower labour and land costs and a larger pool of job seekers.

  For example, early in 2008 Hong Kong sweater maker Milo's Knitwear opened a factory in Jiangxi province, some 650 km from Hong Kong, where operational costs are about 20% lower than in nearby Dongguan.

  Another famous setup in Dongguan, Dongyue Garment Factory, has relocated one of its workshops to Heyuan City in the north east of Guangdong province and another one to Hubei province.

  Other companies are relocating production to cheaper Asian countries like Vietnam, Cambodia and Indonesia, and even to commercial hub Dubai, where Chinese workers are reportedly flown.

- Shift in marketing focus from export markets to domestic markets. According to the China National Textile and Apparel Council, China's domestic clothing demand in 2007 rose by 32%, 14.5 percentage points higher than the general growth in consumables.

  It's also noteworthy that Western retailers are betting on soaring clothing consumption and growing quality and brand awareness in China.

  Early October 2008, Marks & Spencer opened a 3,800 square metre flagship store in Shanghai. Brands such as Zara, H&M, Muji, C&A and American Apparel also have a presence in China, while luxury brands like Gucci and Prada cater to the wealthy.

- Shift in exports from US and EU markets – thought to be in preparation for any new measures to curb imports from China in 2009 – to neighbouring Asian countries and even to South American markets.

- Shift from 'Make' to 'Create'. Many firms in Southern China's apparel producing centres, like Shenzhen, Dongguan and Guangzhou, are planning to shift their production model from 'make' to 'create'.

  In an effort to encourage local manufacturers to develop brand names, the Dongguan treasury department has allocated RMB67m (EUR7.8m) to reward those designated "famous brand enterprises".

  The shining role model for Chinese manufacturers who dream of their own brand is 'Aimer', China's top high-end lingerie company in terms of employment (3,000 staff), sales (US$90m in 2007) and consumer awareness.

- Shift from labour-intensive production to technology- and capital-intensive production.

  This is the strategy of Hong Kong based TAL Apparel, one of the world's largest contract clothing producers whose customers include JC Penney, Calvin Klein, Debenhams, Giordano, and Liz Claiborne.

  Last year TAL started up a new US$70m factory in Dongguan, and it plans to double the size of the factory in 2009.

- Guarantee product quality and the manufacturing process, including social compliance.

  The China National Textile and Apparel Council is co-operating with the Foreign Trade Association in Brussels, the European Commission, the US-based Worldwide Responsible Accredited Production (WRAP) and many retailers to build a responsible international supply chain.

- Co-operation between companies. In a joint initiative last year, eight textile dyeing and printing plants in Dongguan invested around US$4.5m in a water processing plant.
- Avoid price competition. In Haining (100 km from Shanghai), a city that claims to represent 25% of China's warp knitting industry, a price index system has been established to allow companies to adjust the pricing of their products to avoid "vicious price competition."

The last edition of Intertextile Shanghai Apparel Fabrics, the China International Trade Fair for Apparel Fabrics and Accessories, took place from 20-23 October 2008, attracted 2,559 exhibitors and 49,000 buyers. The next event will be held from 20-23 October 2009.

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